

## **Maryland Business Tax Reform Commission Business Tax Reporting Subcommittee**

**Key Responsibility:** Investigating and analyzing the pros and cons of business tax reporting regimes in the context of Maryland’s economy pursuant to the statutory charge in Special Session legislation.

### **Business Tax Reporting Subcommittee Charge - Summary**

This subcommittee will address the statutory directives of “*recommendations for changes to the State’s business tax structure to provide for fair and equitable taxation for all corporations and other business entities doing business in the State,*” and specifically: (i) “*the imposition of combined reporting using the ‘water’s edge method’ under the corporate income tax for unitary groups of affiliated corporations,*” and (ii) the “*imposition of other types of business taxes, in lieu of or in addition to the current taxes imposed, including gross receipts taxes, value added taxes, and alternative minimum taxes.*”

### **Members:**

#### **Chairman Wacks**

Paul Nolan

Karen Syrylo

Michael Ettlinger

Senator Nancy J. King

Martin Lobel

Delegate D. Page Elmore

Delegate Kumar Barve

Secretary T. Eloise Foster

Other Attendees

### **Timeline:**

October – April – Subcommittee Meetings (include at least one for public testimony)

#### **• Overall Structure of Subcommittee Activity**

- Subcommittee will meet every other Thursday (2x’s per month), except during the General Session, when meetings will occur late Monday afternoon
- 2 hour meetings
- Separate Subcommittee analysis into segments
  - 2 – 3 meetings per topic
    - Education / Knowledge Base – to provide the opportunity for each Subcommittee member to develop

an understanding of how each reporting regime operates

- Discussion
- Develop Findings – Pros / Cons (i.e., written materials will be developed by the Subcommittee throughout the process)

- **Chronology of analysis of Topics**

- November / December – Separate Reporting (including business flow through taxes )
  - History & Fundamentals of a Maryland separate return (overview)
  - Brief demonstration of sample calculations of a separate return and a combined return
  - Detailed review of methodology and calculations used in the October 1, 2009 Comptroller’s analysis of impacts had combined reporting been in place in tax year 2006
  - Walk-through of 2004 Amendments and other enforcement improvements to address tax avoidance, detailed discussion of Maryland separate returns
  - Discussion of tax avoidance strategies that may still be in place and methods to address them
  - Discussion of current tax rate and whether it is appropriate
  - Apportionment
  - Nexus
  - Administrative and Compliance issues
  - Pros / Cons
- December / January – Combined Reporting
  - History & Fundamental of a combined return
  - Unitary group concepts
  - Apportionment
  - Nexus – Determining a Combined Group
  - State Net Income Calculation
  - Economy – past / present
  - Transitional issues
  - Administrative issues – costs of transition and Compliance issues
  - Pros / Cons

- January / February – Alternatives to Income Tax
  - History & Alternative approaches (gross receipts tax, value added tax, base broadening, etc.)
  - Nexus
  - Calculation – inclusions / exclusions
  - Transitional issues
  - Administrative issues – costs of transition and Compliance issues
  - Pros / Cons
  
- March / Early April
  - Public Testimony as Necessary
  - Discuss Pros /Cons of Findings
  
- Late April / Early May
  - Draft Report
- Late May / Early June
  - Final Report to full Commission

**Knowledge Base:**

- COST Materials
- Reading materials submitted to Chairman Wacks and subcommittee members in advance for preparation.
- Presenters / Educators at meetings – consultative function.

**Minutes / Notes –**

Minutes will be kept for each meeting to be published on the Maryland Business Tax Reform Commissions’ Website. This will enable participants who are not able to attend meetings to virtually attend the meetings, as the published minutes of the meetings will in effect, make the meeting transparent.

**Draft & Final Report –**

To be discussed in Subcommittee – members should volunteer to draft pieces of the Report for discussion / review of the subcommittee. A process for drafting and finalizing the report will need to be implemented.

## **Business Tax Reporting Subcommittee Charge - Detailed**

This subcommittee will address the statutory directives of “recommendations for changes to the State’s business tax structure to provide for fair and equitable taxation for all corporations and other business entities doing business in the State,” and specifically: (i) “the imposition of combined reporting using the ‘water’s edge method’ under the corporate income tax for unitary groups of affiliated corporations,” and (ii) the “imposition of other types of business taxes, in lieu of or in addition to the current taxes imposed, including gross receipts taxes, value added taxes, and alternative minimum taxes.” This subcommittee will achieve this by examining the following possible business tax reporting regimes:

- a. Status Quo – Separate Reporting enhanced by the 2004 law changes to address abuse.
- b. Combined Reporting
- c. In particular, the Subcommittee will consider the pros and cons of:
  - A. Whether Combined Reporting reflects a more accurate measure of income than Separate Entity Reporting.
  - B. Whether and to what extent Combined Reporting addresses income shifting that current law Separate Reporting in Maryland has not already addressed?
  - C. The administrative complexities and costs associated with a transition to Combined Reporting, including costs and transitory issues related to compliance.
  - D. The definition(s) of a “Unitary Business” in Maryland if Combined Reporting were to be adopted.
  - E. The composition of taxable income, i.e., Finnegan (whole) vs. Joyce (entity by entity) approach
  - F. Transition issues to include the use of NOLs and other modifications accrued in years prior to enactment, Finnegan entity tax credits/NOLs, etc.
- d. Alternatives to Corporate Income Tax - Subcommittee will examine the imposition of other types of business taxes, in lieu of or in addition to the current taxes imposed, including gross receipts taxes, gross margin, value added taxes, tax base broadening (sales tax), and alternative minimum taxes.

- e. Business Flow Through Taxes – The subcommittee will examine business income taxes generated through flow through entities including S Corporations, LLC's and Partnerships (Flow-Through) which are reported on individual income taxes. Included in their examination are the following topics:
- A. How much business income is reported on an annual basis and reported as a consequence of Flow Through businesses on Individual Income Tax Returns?
  - B. How much business taxes are paid through Individual Returns and what the average tax rate is?
  - C. How many Individual Returns report more than one flow through business entity?
  - D. A comparative analysis of the relative tax burden for small, mid and large size businesses in Maryland in Corporate and Flow Through Form.
  - E. The calculation of the "credit for taxes paid to other states" results in the Maryland resident owner of a multistate S-corp, LLC etc. paying Maryland's county income tax on income that was generated and taxed in other states (no "credit" is given against the county tax).
  - F. Pros and Cons of unique business taxes to apply to Flow Through entities

**Governance Structure:**

- Each Subcommittee will identify, analyze and document the pros and cons of the aspects of the reporting regimes and business incentives described above without making a specific recommendation. This approach is intended to encourage the production of ideas and materials that will assist the Commission in reaching its recommendations.
- Each Subcommittee will present this analysis for consideration by the full Commission which will determine the recommendations to be made in Commission reports.
- While each Commission member will be assigned to one Subcommittee, all Commission members are welcome to participate in both Subcommittee activities if they choose to devote the time.